EXHIBIT A

UNITED STATES OF AMERICA

Before the

Federal Power Commission

Washington, D. C.

In the Matter of Pacific Gas and Electric Company	**Docket No. E-6482**

Reply Brief of Pacific Gas and Electric Company

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SUBJECT INDEX

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INTRODUCTION

In this brief Pacific Gas and Electric Company, seeking authority to increase its rates for electric service to Sierra Pacific Power Company, replies to the brief of the latter company opposing the increase. As in the opening brief the parties will be referred to as Pacific and Sierra, respectively. Since the brief of the Commission's Staff concludes that Pacific has met the burden of proof, imposed upon it by the Federal Power Act and by this Commission's order, to show that the proposed rate is just, reasonable and not unduly discriminatory or preferential this reply will be

directed entirely to Sierra's brief. However, to the extent that the Staff's brief seems to accept, without discussion, some of the contentions of Sierra, this reply is intended to apply to the Staff's brief as well.

STATEMENT OF THE ISSUES

Comparison of the three opening briefs on behalf of Pacific, the Commission's Staff and Sierra reveals agreement on a number of primary facts and principles of law.

It is not disputed that under the present schedule of charges Pacific will receive only a 2.6% return on its net investment in all facilities allocated to service to Sierra. It is stipulated that Pacific is entitled to a 5.5% return for its electric department (T. 675).* Thus Pacific's service to Sierra is producing revenue which yields less than one-half of what would be a fair rate of return. It is also undisputed that the increased charges proposed by Pacific will produce only 4.75% return, a rate of return still well below that stipulated to be reasonable.

The Staff's brief finds that the proposed rate is just and reasonable when measured by the cost of service including return at 5.5%, and concludes that there is nothing to justify departure from that standard as a measure of the reasonableness of the rate (Staff's Brief, p. 34).

To avoid any contention of discrimination against Sierra, Pacific has proposed a rate which will yield only 4.75%, the proposed tariff being equivalent to Pacific's Schedule F. P. C. No. 6 (Supplement No. 1) for service to The California Oregon Power Company and also equivalent to

* References thus are to pages of the transcript of the hearing on this matter.

Pacific's regular filed tariff for intrasate resale service. Neither Sierra nor the Commission Staff find the proposed rate to be unduly discriminatory or preferential (Staff's Brief, p. 31; Sierra's Brief is silent on this point).

Since the reasonable rate of return is 5.5%, to require Pacific to continue to serve Sierra for a return of only 2.6% would amount to confiscation of investment in excess of eight million dollars devoted to service to Sierra.[1]

In the face of this obviously confiscatory return Sierra argues that it is in the public interest to require that the present rate remain in effect, "at least as long as Pacific earns more than it would save if Sierra's business were lost or abandoned." This contention requires the assumption that Pacific deliberately entered into a contract in 1948 by which it committed itself to a transmission line investment of more than one million dollars, and agreed to make an additional transmission line investment of similar amount when Sierra's load should require, all on the basis that it would not be *entitled* to any return or depreciation on the investment over a period which may extend until 1979!

This assumption is directly contrary to common sense and to the testimony of both parties that the purpose of the 15-year term of the contract was to protect Pacific's (and Sierra's) investment in transmission lines to be constructed in accordance with the contract for the service to Sierra. Sierra's strained argument simply ignores this fact and fails completely to explain how a rate so long as to be confiscatory is consistent with protection of the investment.

[1] The California Public Utilities Commission, herein called California Commission, in fixing rates subject to its jurisdiction has not permitted Pacific to recover any revenue from other customers to offset the present low return from Sierra.

It is obvious that Pacific could not even recover the cost of borrowed capital to make this investment, let alone provide anything for equity money on such a rate of return.

Without this assumption of a commitment by Pacific to perpetuate the present rate Sierra's arguments have no foundation. This brief will show that there was no such commitment because (1) it is contrary to the terms of the contract both as expressed in the contract and as contemporaneously interpreted by the parties, (2) it is not to be implied from adoption of a schedule of charges equivalent to Pacific's 1945 Schedule P-31 for intrastate resale service, and (3) it is not to be implied as a consequence of the fact that Sierra made the contract with Pacific in preference to a contract for Bureau of Reclamation power which could not be delivered when needed.

The Staff's brief concludes that even if such a commitment were made it should have no bearing on the result since the principle involved is contrary to the public interest. With this we are in accord since a contract requiring such a large additional investment for public utility service which does not permit a recovery of a reasonable return on the investment would be clearly unreasonable.

If Pacific had made a contract on such an improvident basis the Federal Power Act would require this Commission to determine the reasonable and just contract to be in force hereafter (Sec. 206 (a)). However, the evidence demonstrates that Pacific did not make such an ill-advised contract but clearly contracted for protection of its investment and we need not pursue the point further here.

As we understand Sierra's position—and it takes considerable analysis to disentangle the structure of its argu-

ment from its so-called "Abstract of Evidence" and the subdivisions of its "Argument"—this Commission is not bound by a rule of law in this case but is to act on the basis of its determination of the requirements of the public interest. Sierra has virtually abandoned its procedural point, urged in a barrage of petitions and motions demanding a termination of this proceeding as a matter of law, and has conceded that all of the issues are now before this Commission for determination. We would add only that the measure of the public interest is found in the requirement of the Federal Power Act that all charges demanded or received by any public utility "shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful" (Sec. 205(a)).

We submit that a rate of return of 2.6% is not just or reasonable but is confiscatory, and that an increase to 4.75% is justified and reasonable under all the circumstances. We turn now to our reply to Sierra's attempt to argue the contrary.

I.

SIERRA AND PACIFIC AGREED ON A TERM CONTRACT SUBJECT TO CHANGE BY REGULATORY PROCESS FOR PROTECTION OF THEIR ADDITIONAL INVESTMENTS IN TRANSMISSION FACILITIES.

A. This Commission Has Jurisdiction to Change the Present Contract Rate.

Sierra concedes, as it must, that the present service contract is subject to such changes as this Commission may direct in the exercise of its jurisdiction (Sierra's Brief, p. 50). If, as Sierra indicates, this must be deemed an express provision of the service contract, then it is difficult to see how Sierra can contend that the parties contemplated an

unchangeable rate. Indeed, we suppose that if Pacific's cost of service to Sierra had declined sufficiently Sierra would have demanded and been entitled to receive a reduction in the rate.

It is interesting to note that Sierra's brief nowhere states that Pacific *agreed* that the rate should remain unchanged for the entire contract term. Such a proposition too obviously flies in the face of the facts.[2] Yet, paradoxically, Sierra also contends by argument in its "Abstract of the Evidence" (pp. 30-31) and in its Point I (p. 48) that Pacific is committed to an unchanging rate. If all that Sierra means is that the present rate was intended to remain fixed until changed by the rate making process we do not quarrel with its position. Pacific has never contended that it had any arbitrary power, or, independently of regulatory process, any power at all to change its rate to Sierra. On the other hand, Pacific has always intended and understood that it may initiate a change in its rate to Sierra, just as in any other rate, through established regulatory procedure. That is exactly the course which it has followed here. The implied reservation to the Federal Power Commission of authority to modify the contract is the basis for Pacific's action.

Pacific does not claim to be able to place in effect any increase in its charges to Sierra unless it sustains its burden of establishing before this Commission that the increase is just and reasonable in a proceeding which gives full opportunity to Sierra to be heard and to oppose the increase if it chooses. In the light of fair analysis Sierra's attempt to argue by epithet that change by this process is "repudia-

[2] See Pacific's Brief, pp. 21-25.

tion''[2a] or renders the contract ''nugatory and valueless'' becomes baseless accusation. Similarly, for Sierra to argue that its management cannot conduct its business on the basis of a contract subject to change by regulatory process is to deny the experience of every electric and gas utility dependent upon wholesale purchase for its supply of energy and gas.

B. Pacific Did Not Give up Its Right to Invoke the Rate Making Process to Increase Its Rate to Sierra.

Sierra could not concede, however, that the service contract is subject to change in the normal course of regulation without undermining its case. If Pacific could invoke the normal regulatory process for a rate increase Sierra could not claim that Pacific had voluntarily assumed the burden of increasing costs. It therefore attempted to prove that Pacific gave up this right when it executed the service contract without an express provision that the rate was changeable by the normal rate making process (Sierra's Brief, p. 48). We would have thought that the express and implied reservations of authority to the California and Federal Commissions to change the contract (Sierra's Brief, p. 50) were adequate expressions of Pacific's intention but Sierra ignores them. Instead Sierra attempts to draw a conclusion from comparison with Pacific's Schedule F.P.C. No. 6 for service to The California Oregon Power Company. That

[2a] The term "double dealing repudiation" which counsel for Sierra has seized upon so enthusiastically was used by counsel for Pacific only with reference to a contract with the City of Redding made about four months before the filing of the rate increase application from which the contract was voluntarily excepted by Pacific. This contract was made after a public election in Redding in which the voters expressed their choice for a contract with Pacific in preference to a concrete proposal from the Bureau of Reclamation. See California Public Utilities Commission Decision No. 43147, issued July 26, 1949 (not printed).

schedule contains a formula provision for adjustment of the rate to correspond with changes in Pacific's regular filed resale tariff for intrastate service.[3] It should be evident that this formula, incorporated in a 1952 contract after Sierra had contested the right of Pacific to obtain a rate increase, was adopted to forestall the argument made here. It cannot aid in the interpretation of a contract made four years earlier when there was no such contest.

It is even weaker for Sierra to argue (its Brief, "Abstract of the Evidence," p. 31) that the fact that a comparison was made by Sierra between Pacific's present rate and the Bureau of Reclamation's proposed rate for a 15-year period evidenced any intention or understanding that that rate could not be changed. This comparison was the only one that could be made between the two rates since future changes in the cost level could not be predicted. It would be absurd for Pacific to argue that the present rate could not be reduced by this Commission for 15 years simply because Sierra had made a 15-year comparison on the assumption of no change in rate level. It is equally absurd for Sierra to argue that for such a reason there can be no increase when fully warranted by increased costs.

Sierra attempts to bolster these arguments with references to testimony given in 1945 before the California Commission by Pacific's rate engineer. We will discuss them in a subsequent section of this brief since they relate to the adoption of the P-31 rate for intra-state resale service and form no part of the understanding between Sierra and Pacific as expressed in their 1948 contract.

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[3] We do not assume that this formula is binding on the Federal Power Commission. Most of the energy delivered under the California Oregon contract is resold by the purchaser within California.

C. The Contemporaneous Evidence Demonstrates That the Purpose of the 15-Year Term of the Contract Was to Protect Pacific's Investment.

We need not rest our case on the weakness of Sierra's arguments. The direct and positive evidence of the contract itself and the virtutally contemporaneous statements in the 1948 hearing before the California Commission prove that the purpose of the 15-year term was protection of the new investment.

Two prior contracts, each of which called for a new transmission line, had 15-year terms. Pacific's first proposal to Sierra in 1947 was for a new line and a new 15-year term. The 15 years was accepted without discussion throughout the negotiations and without relation to the rate.

It is significant that the contract relates the 15-year term to the completion of the new 110,000 volt line and requires a new 15-year term to begin when a second such line is completed and placed in operation to meet Sierra's requirements.

When to this internal evidence of the contract is added the statements of both parties made before the present controversy arose there can be no doubt that the term of the contract was intended to protect their respective investments. As to the reason for the 15-year term, Mr. Pollard testified for Pacific before the California Commission in 1948:

> "Well, of course, that was—on our part was in order to guarantee that we would have business for a long enough period of time *to warrant us in making the investment** in the cost of the new line and amortizing it. And, furthermore, followed the same pattern as

* Emphasis ours, throughout the brief.

previous contracts we have had in each of which instances a substantial investment was made for service of this customer. And, similarly, 15-year contracts were taken at each of those times for that reason." (Ex. 12, p. 12)

In the same proceeding Mr. Tracy testified for Sierra on the necessity for a 15-year contract.

"When load conditions are such that you have to have additional capacity it might be that that additional capacity could be arranged to carry you over for a short period—be sufficient to carry you over for a short period, but in case where you have to go to a relatively large investment it is only fair and business —proper business that the Company you are negotiating with *gets a proper return on the investment for that period.* That is the basis upon which we would operate ourselves, we would not expect anybody to go to a large investment which is necessary in order to give the Company capacity they need for any shorter period than that." (Ex. 12, p. 26)

In the same proceeding the following occurred on cross-examination of Mr. Tracy:

"Q. This contract effectively tie Sierra's hands for 15 years, will it not?

A. In what way do you mean?

Q. Well, because of the fact that you are prohibited from developing any further power facilities of your own?

A. No, I do not think that is true. The contract is worded in that way, if the parties have a modification that is justified I think the parties can get together on it. In other words, only the—the principal thing that the selling party would have—I might be corrected on this if I am wrong from P. G. & E. Company—would be

> idle investment. In other words, if we had a development that we found feasible and it came in at a time when any investment was [not][4] made idle by the P. G. & E. in other words, at a times when they might have to put in additional investment even to serve it, it would not penalize P. G. & E. if we went ahead on it and we could make arrangements with them to do so." (Ex. 12, pp. 33, 34)

In other words Mr. Tracy believed that Pacific's primary concern was its investment and that a modification of the contract for Sierra's benefit would be justified under any circumstance where Pacific's investment was protected. If Mr. Tracy had exhibited the same reasonable attitude which he expected from Pacific in 1948 toward Pacific in 1952 when requested to renegotiate the present rate in accordance with the order of the California Commission[5] this proceeding would doubtless have been unnecessary.

In the present proceeding in 1953 Mr. Tracy testified that in his 1948 testimony before the California Commission he gave all the reasons which he could think of in support of the contract (T. 672). The transcript of that proceeding (Ex. 12), will be scanned in vain for any indication that Pacific intended to give up any right to initiate a rate increase or that Mr. Tracy ever had any such understanding. Are we to believe now that it was mere oversight that when the 15-year term was mentioned in 1948, Mr. Tracy thought only of a proper return for Pacific's investment rather than a guaranteed rate for Sierra, even though he was obviously looking for reasons to satisfy his Nevada opposition?

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[4] The context requires insertion of the "not" at this point.

[5] Exhibit 17, pp. 41, 46-47, and T. 987, 988.

Not quite two years later, before the California Commission in 1950, Mr. Moulton, Pacific's Vice President and Executive Engineer, explained the difference between the 15-year term of the Sierra contract and the 5-year term of other resale contracts as follows:

> "We finally made a 15-year contract with Sierra Pacific. *We made a longer contract because we under-*[*took*][6] *to build an additional line* to supply them and *we felt we needed that protection of a long contract.*" (Ex. 15, p. 541)[7]

Even in 1952 after Sierra had determined to oppose any increase by Pacific, Mr. Tracy testified for Sierra before the California Commission on cross examination as follows:

> "Q. While the Commissioner has stated that the record in the contract proceedings contains the support for the contract or purportedly it did, you made the statement that you made this 15-year contract because you wanted to have assurance of power supply and that it was the best source of power at reasonable rates. Is it not a fact, Mr. Tracy, that Pacific Gas and Electric Company was insisting on a 15-year contract in order to protect it in a very large investment that it had to make in facilities in order to bring power to the summit to supply to the Sierra Power Company?

[6] The text has "understood" at this point, clearly a reporter's error.

[7] This testimony also shows that Sierra is completely mistaken in interpreting Mr. Moulton's testimony as support for its position that the contract rate could not be changed. Mr. Moulton recognizes that the purpose of the 15 year term was to protect the new investment. This testimony was given within a few months after initiation of service over the new 110,000 volt line to Sierra, and the fact that an increase was not deemed warranted at that time does not constitute a bar to an increase under conditions of greatly increased cost.

A. I think that works both ways. Yes, our company wished to have a firm contract too to cover our investment." (Ex. 23, pp. 1418, 1419)

Protection of investment is not accomplished by ignoring diminishing returns. Failure to allow a fair return on property devoted to public utility service is confiscation of that property. To argue that Pacific consented to possible loss of all return for up to 30 years on a new investment in excess of one million dollars is absurd and contrary to the express testimony.

We submit that the evidence establishes without contradiction that Pacific did not give up its right to a rate increase by means of normal regulatory procedure and that it is entitled to a rate of return which will protect its entire investment for service to Sierra.

II.

THE ADOPTION IN THE SIERRA CONTRACT OF CHARGES EQUIVALENT TO THOSE IN PACIFIC'S INTRA-STATE RESALE TARIFF P-31 DOES NOT SUPPORT SIERRA'S CONTENTION THAT PACIFIC COMMITTED ITSELF TO PERPETUATE THAT RATE FOR THE CONTRACT TERM.

When the present contract was being negotiated with Sierra in 1947 and 1948 Pacific had on file with the California Commission two tariffs of general application for intra-state resale electric service to customers who purchased all of their energy requirements from Pacific. One of these, Schedule P-31 (Ex. 20), offered a rate approximately 10% below the other (Schedule P-6, Ex. 8, p. 2) to resale customers who would enter into a five year contract for service. The contract with Sierra did not incorporate the P-31 rate as such. It simply provided a

schedule of demand and energy charges equivalent to those in effect under the P-31 tariff, plus a stand-by charge, and incorporated certain of the conditions of that tariff.

A. The P-31 Rate Was Not a Fixed Rate But Was Actually Increased Twice by the California Commission.

Sierra would argue first that the P-31 rate was established as a fixed rate for the term of each five-year contract and therefore that the Sierra rate is a fixed rate for the 15 to 30 year term of its contract. We have already shown that the conclusion does not follow because the 15 year term was proposed for protection of the new investment long before the P-31 rate entered into the negotiations. The premise that the P-31 rate could not be changed is equally unsound.

The California Commission has twice increased the P-31 rate since its adoption in 1945. The first occasion was in 1950 in response to Pacific's application for a 6% rate increase. The second occasion was in 1952 when the California Commission superseded Schedule P-31 by Schedule R, which is equivalent to the rate proposed in this proceeding. In each of those cases the Commission excepted from the increase certain named customers but the balance were required to pay the increased rate beginning with the effective date of the general increase regardless of the fact that they were being served under term contracts.[9] This

[9] As to the 1950 increase of 6%, Exhibit 18 shows that Pacific requested an increase in each of its filed schedules (p. 8) and was authorized to make such increase effective for service from April 15, 1950 subject only to the named exceptions (p. 16). Pacific estimated that it would receive additional revenue of $140,000 annually from resale customers as a result of this increase (p. 8).

As to the 1952 increase, Exhibit 17 shows that the California Commission authorized cancellation of all existing schedules and

is convincing evidence that the California Commission does not regard the P-31 rate as immune from changes when required by increases in the cost level.

The testimony of Pacific's rate engineer in 1945, to the effect that users of the P-31 rate were assured of the lower rate for a five-year term (quoted by Sierra in its brief at pp. 31, 49), sounds impressive when isolated from its context. We believe, however, that a study of the record of that proceeding will show that Mr. Beckett meant "lower than the P-6 resale schedule" and that he did not have in mind a fixed rate regardless of cost considerations. In any event the California Commission has set the matter at rest by granting the increases above described.

B. Pacific Did Not Give Its Right to a Compensatory Return When It Offered the Equivalent of the P-31 Rate.

The adoption of the P-31 rate level is also used by Sierra as the ground for a contention that Pacific committed itself to a non-compensatory rate level. Sierra argues that because the P-31 rate was conceded in 1945 to be non-compensatory when applied to a class of resale customers which did not include Sierra, therefore Pacific committed itself to a non-compensatory return from Sierra by adopting the same rate level. It should be obvious, however, that the

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transfer of customers to the increased schedules applicable to the service rendered, including Schedule R for resale customers (pp. 46, 85) subject only to exception for certain listed contracts.

The exception of Sierra from the 1952 increase was expressly stated by the California Commission to be for the purpose of allowing an opportunity for the parties to renegotiate the contract "in the light of the new basic resale schedule," i.e. Schedule R (Ex. 17, p. 41). The refusal of Sierra to negotiate (T. 988) does not convert this exception into a final disposition of the matter by the California Commission. The matter is pending before that Commission in a new proceeding. See Exhibit 22, pp. 4 and 5.

statement as to the return from a given rate when applied to a certain class of customers is not necessarily true when the same rate is applied to another customer under different circumstances. In 1952 Pacific was able to earn a 2.6% return in its business to Sierra in spite of the sharp increase in costs subsequent to 1948. It should be evident that on the basis of 1948 costs Pacific must have anticipated a reasonable return.

There is no concession in the 1948 proceedings before the California Commission that the Sierra rate was expected to be non-compensatory. A California Commission staff member asked Pacific's witness whether, *if* the rate should prove non-compensatory, no burden would be placed on other customers. Pacific's witness agreed that under such circumstances other customers should not be burdened. We do not see how this can be taken as evidence one way or another as to how much return the Sierra rate was expected or intended to produce, nor as evidence that Pacific's stockholders did not expect to be fairly compensated from Sierra's business.

This Commission will realize, however, that while the new line remained lightly loaded it would hardly be likely to earn a full return. This, however, should not prevent realization of the full earning power of the line as utilization increases. The Staff's method of deriving cost of service and rate of return by averaging in with the system network the special lines devoted to service to Sierra eliminated from consideration the actual loading of these lines and the present 2.6% return thus computed does not reflect any particular stage in the growth of Sierra's load.

C. The Proposed Rate Meets Sierra's Test Since Pacific Will Not Receive More Revenue Under the Proposed Rate Than It Could Save by Abandoning Sierra's Business.

Throughout its argument Sierra is careful to qualify its contention as to maintenance of the present rate by conceding that Pacific is entitled to earn at least as much under the present rate as it would save if Sierra's business were lost or abandoned. We have already pointed out in our opening brief (pp. 29-32) that this reasoning is applicable only to a rate designed to retain existing business served by facilities which otherwise would be idle, and that it does not apply where a substantial additional investment is contemplated. However, even taking at its face value Sierra's test which compares revenues under the proposed rate with the costs which Pacific could save if it abandoned Sierra's business today the rate will qualify.

All of Pacific's investment in generation and transmission capital allocated to Sierra could be used almost immediately to serve other customers on Pacific's system, excepting only the three transmission lines from Drum to Summit. Pacific's load has been increasing at a rapid rate for many years and it is still engaged in expanding its generation and transmission capacity to meet the growing demands on its system. The increase in Pacific's sales of energy during 1952, as shown on page 69 of Pacific's Form 1 report to this Commission for that year, was 3.75 times the entire amount of Sierra's load for the year. Loss of Sierra's business then would simply mean freeing capacity for use elsewhere on the system.

The rate base allocated to Sierra by the Staff method (Ex. 19) consists almost entirely of generation, transmission and common utility plant and includes only 1.4% of

the $1,861,765 invested in the three transmission lines used to serve Sierra. This results from the fact that the investment in these lines is treated as part of the system network, 1.4% of which is allocated to Sierra.

It follows that the cost of service derived by the Staff's method does not include more than a negligible amount for depreciation or return and related income tax on the investment in the three transmission lines. To put the matter in another way, if Pacific should lose Sierra's business today, substantially all of the $8,489,633 of capital investment allocated to Sierra would shortly be used to serve other system load and would be expected to earn a fair and reasonable return.

The same result will be reached if Sierra's erroneously conceived test is applied to Pacific's derivation of a rate of return (Ex. 4). In Pacific's computation the investment in the three lines is allocated directly to service to Sierra and all of it appears in the rate base. The revenue under the proposed rate falls short of full costs of service by $725,000 per year, a deficiency far in excess of any conceivable depreciation, return and related income tax allocable to the three lines. See Pacific's Brief, pp. 6, 7 and Appendix.

The conclusion of counsel for Sierra that the fact that Pacific earns some return shows that it is earning more than it could save if it lost the business is a superficial conclusion not supported by an analysis of the rate base on which the return is earned. On the contrary, it must be concluded that from the standpoint of Sierra and its customers, the proposed rate is as low as could reasonably be permitted by any method of cost calculation and by any test which has been suggested.

III.

THE EXISTENCE OF PUBLIC PRESSURE UPON SIERRA TO CONTRACT FOR BUREAU OF RECLAMATION POWER WHICH COULD NOT BE DELIVERED WHEN NEEDED DOES NOT JUSTIFY THE CONTENTION FOR A RATE FIXED REGARDLESS OF COST.

A review of the record in this case and the three opening briefs will show that "competition" is a word of many meanings. Counsel for Sierra profess amazement that we should deny the existence of competition with the Bureau of Reclamation, whereas we fail to see how they can label a situation competitive when the consumer has only one feasible source for the supply of its needs. Despite this diversity of opinion as to what constitutes competition there is substantial agreement as to the facts of the situation and we propose to talk about those facts.

The first fact is that Sierra needed a substantial amount of additional power to meet its load requirements in 1949 and 1950.

The second fact is that the Bureau did not even hope to obtain appropriations from Congress and complete a single circuit line to serve Sierra before 1951 and probably not until 1952. The Bureau of Reclamation thus had no way of supplying Sierra's 1949 and 1950 requirements for additional power.

The third fact is that Bureau power as a source of supply for Sierra would have had many disadvantages even after service was initiated. Chief among these were (1) reliance on 125 miles of single circuit line, (2) reliance on a single hydroelectric project which could be affected by adverse water conditions, (3) requirements for standby service at

"prohibitive" additional cost (Ex. 12, pp. 28, 31), and (4) the Bureau requirement that Sierra "wheel" power to municipalities and public agencies entitled to "preference" under reclamation law (Ex. 21, p. 17, par. ii).

The fourth fact is that in 1947 and 1948 there was considerable agitation in Northern and Central Nevada to get "cheap" government power. Public sentiment was aroused and Sierra was under pressure to make some sort of arrangement for obtaining power from the Bureau of Reclamation.

These facts are not disputed and whether counsel for Sierra labels the Bureau as a "competitive" source of power is really immaterial. The label adds nothing, but when counsel try to argue that Sierra lost a bargaining position when it entered into the contract with Pacific they have to insist on the label and ignore Sierra's actual situation. Realizing, however, that the facts are inescapable, they try to make it appear that Sierra had a choice between two feasible sources of supply. To do this they have resorted to invention.

That awkward gap between 1948 and 1951 in Sierra's power resources, if it chose to contract for Bureau Power, is "tided over" (Sierra's Brief, pp. 39 and 66) by counsel's construction of the Walker River development. Since both Sierra's President and its engineer are agreed that construction of that project would have taken a minimum of three years (Ex. 12, p. 34; T. 745), Sierra would still have been short of power in 1949 and 1950, even if it decided to construct the Walker River project in the face of high costs.

The statement of the 1953 Nevada Public Service Commission (Ex. 22, p. 2) containing its views as to the position

of the 1948 Commission,[10] suffers from the same infirmity as the argument of Sierra's counsel. That Commission now states that if it had, in 1948, doubted the "validity" of Sierra's contract it would have ordered Sierra to construct hydroelectric plants on three rivers and a supplementary steam plant. Thus Sierra would have had to invest unknown millions of dollars in high cost hydro plants and a steam plant to be operated at low load factor with high fuel costs,[11] none of which could have been constructed in time to meet its 1949 and 1950 requirements. While we doubt the authority of the Nevada Commission to issue such an order we doubt even more that in 1948, faced with the practical requirements of the situation, it would have seriously entertained such an idea.

Disregarding the time required for construction of new plants and disregarding their high cost of construction and operation, counsel for Sierra reach new heights of economic absurdity when they contend that these additional plants would have been developed "to tide over the expected shortages until the Bureau's lines were adequate to meet all possible needs." Neither of Sierra's witnesses testified that capital investment in any of these plants could be justified on a

[10] Neither of the two members of the Nevada Commission who appeared in the 1948 hearings before the California Commission is now a member of the three-man Nevada Commission, according to the letterhead in Exhibit 22.

[11] It will be recalled that Mr. Tracy's opinion that he could produce steam generated power for 7 to 8 mills was based on the assumption (1) that he generated *all* his power requirements in the steam plant and (2) that fuel was at the 1946 Reno price of $2.05 per barrel. It will also be recalled that Mr. Tracy was very much opposed to Pacific's original proposal of a fuel escalator clause. If Sierra operated a steam plant of its own its costs would escalate immediately with each rise in fuel oil prices.

"tiding over" basis, nor did they give any explanation at all as to how the shortage in 1949 and 1950 could have been met.

The fact of the matter is that although counsel for Sierra is correct in stating (Sierra's brief, p. 19) that in October 1947 Sierra had before it a proposal from Pacific and a "plan" of the Bureau of Reclamation and the Colorado River Commission, the latter "plan" fell so far short of meeting Sierra's needs that Sierra never did make a serious endeavor to find out whether, or at what cost, the deficiencies in the Bureau's plan could be made up.

Nor did Sierra ever act like a buyer playing one competitor against another. Mr. Tracy explained to Pacific's General Manager in October of 1947 that his Company was not prepared to continue negotiations, that there was local political pressure to bring Shasta power into Nevada which *hampered Sierra's* negotiation and that Sierra could not afford to offend Shasta power advocates (Ex. 27, p. 4, statement of Pacific's General Manager October 8, 1947 at meeting of President's Advisory Committee). It is evident that Pacific was not given the impression that Sierra found anything desirable in the proposal for Bureau power. Instead Mr. Tracy was making it clear that he was faced with public pressure urging "cheap" government power and ignoring the practical requirements of the situation. The following testimony given by Mr. Tracy during cross examination by Mr. Wahrenbrock in this proceeding illustrates this point:

> "Q. Mr. Tracy, when Pacific Gas and Electric gave up the fuel escalator clause and submitted the proposed form of contract to you after the agreement on the demand and energy charge, what was your opinion as to why they were willing to give up that clause, which would have tended to protect them against at least one of the larger elements of risk in so long a term contract?

[Objection by Mr. Searls on ground of irrelevancy overruled]

* * * * * * *

A. They did not inform me as to the reason and I certainly would not take it upon myself to guess.

By Mr. Wahrenbrock.

Q. Did you think you had outsmarted them on that?

A. No. That isn't the correct answer. We thought that we had showed them sufficient reasons for proposing to us a lower rate.

Q. Namely the threat of taking your load someplace else.

A. The potential competition that was *very prevalent. The papers were full of it.* As I testified before, all the groups were active. The Chamber of Commerce had a power committee." (T. pp. 937, 938)

Notice that Mr. Tracy declined to state that he threatened to take his load elsewhere. To him the word "competition" seems to be synonymous with "public pressure" since he stated in his testimony that even after the contract with Pacific was signed and approved by the California Commission, he was bothered by "competition" (T. 939).

In the face of all this evidence, which boils down to the fact that Sierra could not get the power it needed except from Pacific and the fact that any alternative was bound in the long run to mean high but uncertain costs when all factors were taken into account, Sierra's argument that it gave up a bargaining position or that either it or its customers have lost anything by making a contract with Pacific for service at a rate subject to regulatory change is without foundation.

"The papers were full" of competition and it was "very prevalent," but this sort of competition was more of a problem to Sierra than to Pacific. Sierra had no illusions about

the desirability of a contract for Bureau power as is demonstrated by Exhibits 30, 32, and 34, consisting of intra-company communications which list Mr. Devore's or Mr. Tracy's objections to such an arrangement.

Sierra was not making fine calculations to determine the cost of various alternatives nor was it trying to extract from Pacific an agreement for an unchangeable rate. The 15-year term was important from the investment standpoint but was actually considered objectionable by some public power proponents who did not like Sierra to be tied up for such a period at any price. Sierra endeavored to and did obtain the lowest available rate from Pacific but this was a standard rate, available to qualified resale customers whether or not they had competitive sources of supply.

Pacific undoubtedly felt the effect of the public pressure and reexamined its position that the P-31 rate level was not adequate (Ex. 27, p. 4). When it concluded that it could offer this rate it did not expect that it would be fixed in the face of cost changes. The argument to the contrary seems to be only that because Pacific came down in its price it must be implied that it also gave up its right to the use of the rate-making process. There is no basis for such a conclusion.

When called upon at the California hearing in 1948 to justify making the contract with Pacific, Mr. Tracy attempted to educate the public representatives from Nevada to the facts of the situation which Sierra then faced. He showed that he really had no choice in the matter. He did not claim that the 15-year term was agreed upon to secure a favorable rate; he explained that it was a necessary protection for the new investments to be made. The public representatives were satisfied with this and withdrew their opposition (T. 672).

In a few words, neither Sierra nor public opinion were demanding a fixed rate, nothing in the situation required a fixed rate and nothing in the negotiations, the contract, or the explanations of the contract in the 1948 proceeding ever suggested that a fixed rate had been discussed, much less agreed upon.

CONCLUSION

The issue in this case is whether Pacific's proposed rate increase is just and reasonable under the Federal Power Act. The present rate yields a return so low that its continuance would be confiscatory. Pacific's proposed rate will yield a return of only 4.75%, which is clearly reasonable when compared with the stipulated reasonable rate of return of 5.5%.

Sierra has shown no valid reason why it should be exempted from the increase in costs of generation and transmission of power nor why this Commission should disregard Pacific's need for additional revenue to cover costs of service and maintain its financial integrity.

It is respectfully submitted that Pacific has shown that the present rate is unjust, unreasonable and unduly preferential and that the proposed rate is just, reasonable and not unduly discriminatory. The requested increase should be authorized.

Robert H. Gerdes
Ralph W. DuVal
Frederick T. Searls
Attorneys for Pacific Gas and Electric Company

Wheat, May & Shannon
Robert E. May
Of Counsel

REQUESTED FINDINGS

1. Electric power generated and transmitted by Pacific Gas and Electric Company entirely within California is sold at wholesale and delivered to Sierra Pacific Power Company at Summit in California near Donner Pass under Pacific Gas and Electric Company's rate Schedule F.P.C. No. 3, effective as of January 1, 1948.

2. Sierra Pacific Power Company transmits some of the electric power received from Pacific Gas and Electric Company for sale to customers in California and transmits the balance to its customers in Nevada. By far the larger part of the energy received, approximately 86% in 1951, is thus transmitted to Nevada.

3. The sales of power by Pacific Gas and Electric Company to Sierra Pacific Power Company at Summit are sales at wholesale in interstate commerce subject to the provisions of Sections 205 and 206(a) of the Federal Power Act.

4. Pacific Gas and Electric Company's present rate Schedule F.P.C. No. 3 provides revenue which, after proper allowance for all operating expense allocable to service to Sierra Pacific Power Company, yields a rate of return on the net investment rate base properly allocable to such service which is so low that said rate is unjust and unreasonable and constitutes an undue preference to Sierra Pacific Power Company.

5. Pacific Gas and Electric Company's proposed rate increase contained in its proposed Supplement No. 1 to Schedule F.P.C. No. 3 will provide revenue which is less than is necessary to yield a reasonable return on the net investment rate base properly allocable to the service to

Sierra Pacific Power Company, after due allowance for all operating expense allocable thereto.

6. No other facts have been shown affecting the justness and reasonableness of said proposed rate.

7. The proposed rate is just and reasonable.

8. The proposed rate is not unduly discriminatory or preferential.

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing answer upon all parties of record in this proceeding by mailing a copy thereof properly addressed to:

Howard E. Wahrenbrock, Esq.,
Assistant General Counsel

Drexel D. Journey, Esq.,
Attorney
Federal Power Commission
441 G Street N.W.
Washington 25, D.C.

Winthrop, Stimson, Putnam & Roberts
40 Wall Street
New York 5, N. Y.

FREDERICK T. SEARLS
Attorney for Pacific Gas and Electric Company

Before the

FEDERAL POWER COMMISSION

In the Matter of Pacific Gas and Electric Company	**Docket No. E-6482**

Motion of Pacific Gas and Electric Company for Reopening and Further Hearing

Pacific Gas and Electric Company, hereinafter called PG&E, moves for reopening of this proceeding in accordance with the following:

1. On February 2, 1953, PG&E filed with the Commission its proposed rate schedule Supplement No. 1 to Schedule F.P.C. No. 3 for service to Sierra Pacific Power Company, hereinafter called Sierra. The charges specified in said Supplement No. 1 were higher than the charges provided in said rate schedule F.P.C. No. 3, which latter schedule was in the form of a contract between PG&E and Sierra.

2. The proposed effective date of said Supplement No. 1 was April 6, 1953. By order adopted March 13, 1953, the Commission suspended the proposed rates of Supplement No. 1 until September 6, 1953, and provided that said supplemental rate schedule should go into effect thereafter in

the manner prescribed by the Commission in accordance with the Federal Power Act. By the same order the Commission ordered a hearing concerning the lawfulness of the proposed rate.

3. By order adopted September 25, 1953 and issued September 28, 1953, the Commission declared that the proposed rates of said Supplement No. 1 had become effective as of September 6, 1953, subject to certain provisions of Section 205(e) of the Federal Power Act and made certain orders with respect to accounting and to refund in the event that any portion of the increased rates should be found not to be justified.

4. After hearings held in accordance with said order of March 13, 1953, the Commission, by Opinion No. 270 herein adopted June 16, 1954 and issued June 17, 1954, found that the proposed rate of said Supplement No. 1 was just, reasonable and lawful and, that "if a finding on the lawfulness of the 1948 contract rate were necessary or appropriate, on the record before us that finding would have to be that the 1948 rate is unreasonably low and therefore unlawful;" and in effect by order authorized PG&E to charge and collect from Sierra said proposed increase under Supplement No. 1 to Schedule F.P.C. No. 3.

5. On Sierra's petition to review the Commission's order in said Opinion No. 270, the United States Court of Appeals for the District of Columbia Circuit, on May 23, 1955, set aside the Commission's said order and remanded the case to the Commission with instructions to dismiss the proceeding without prejudice to the initiation of a new proceeding under Section 206(a) of the Federal Power Act.

6. On February 27, 1956, the Supreme Court of the United States on writs of certiorari to said Court of Appeals affirmed the decision setting aside the Commission's said order, but instructed that the case be remanded to the Commission for such further proceedings not inconsistent with the opinion of the Supreme Court as the Commission may deem desirable.

7. On March 30, 1956, PG&E sent its check to Sierra refunding the amount of $382,022.37, which included $336,821.53, the amount of the increase collected from September 6, 1953, the day it was placed in effect, to June 16, 1954, the date on which said Opinion No. 270 and the order therein contained were adopted by the Commission, plus $45,200.84 representing interest thereon at 6% to the day of payment.

8. By motion filed April 16, 1956, Sierra requested the Supreme Court of the United States (1) to amend its instructions upon remand to limit further proceedings before the Commission to the determination of the lawfulness of the contract rate "at the time of such further proceedings" and the fixing of the rate "thereafter to be observed and in force," and (2) to declare that any amounts paid by Sierra in excess of the contract rates were unlawfully collected and that PG&E was obligated to make restitution of the excess payments. On May 28, 1956, the Supreme Court denied said motion without prejudice to the future determination of such rights as Sierra might have to restitution.

9. The opinion of the Supreme Court rendered February 27, 1956, which set aside the Commission's said order in Opinion No. 270, declared in effect that said order would be valid if supported by a finding that the contract rate ad-

versely affected the public interest by being so low that it might (1) impair the financial ability of the public utility to continue its service; (2) cast upon other customers an excess burden; or (3) be unduly discriminatory. Said opinion further declares that whether under the facts of this case the contract rate is so low as to have an adverse effect upon the public interest is a question to be determined in the first instance by the Commission, and that if the proceedings satisfied in substance the requirements of Section 206(a) it would be immaterial that the investigation was not begun under that section.

10. On June 1, 1956, the Supreme Court remanded this case with instructions for such further proceedings consistent with its opinion as the Commission deems desirable. By amplifying and supplementing its findings in accordance with said opinion of the Supreme Court, the Commission will protect the public interest, supply omissions arising from an erroneous view of the law, and make the determinations necessary to establish the right of Pacific to collect and retain the rate of said Supplement No. 1 from and after June 17, 1954.

11. The Commission is, therefore, requested to reopen this proceeding in order to make findings as to whether the rate of said Schedule F.P.C. No. 3 was on and prior to June 17, 1954, and thereafter, so low as to have an adverse effect upon the public interest and whether the rate of said Supplement No. 1 was not in excess of a just and reasonable rate for the service rendered on and after June 17, 1954.

12. Although the record now contains evidence sufficient to support a finding by the Comission that said rate Schedule F.P.C. No. 3 was so low as to have an adverse

effect upon the public interest, PG&E desires to present further evidence in support thereof showing that said rate was, prior to June 17, 1954, and ever since has been (1) so low as to impair the financial ability of PG&E to continue its service to Sierra; (2) so low as to cast upon other consumers an excessive burden; and (3) so low as to be unduly discriminatory. PG&E further desires to present evidence showing that the rate of said Supplement No. 1 was not in excess of a just and reasonable rate for the service rendered on and after June 17, 1954.

WHEREFORE, PG&E prays that this Commission reopen this proceeding to receive evidence, hear argument, and make findings material to the issues herein above set forth as raised by the said opinion of the Supreme Court of the United States and that a date be set for hearing thereon.

Dated this 8th day of June, 1956.

Respectfully submitted,

F. T. SEARLS
JOHN C. MORRISSEY
ROBERT E. MAY
Attorneys for
Pacific Gas and Electric Company

EXHIBIT C

October 1, 1957

Re: Pacific Gas and Electric Company *v.* Federal Power Commission (Sierra Pacific Power Company *v.* Pacific Gas and Electric Company)

Paul P. O'Brien, Esq., Clerk
United States Court of Appeals
for the Ninth Circuit
Post Office Building
San Francisco 3, California

Dear Sir:

You will recall that on September 4, 1957, Mr. Malcolm T. Dungan of Brobeck, Phleger & Harrison wrote to you in connection with possible petitions for review and applications for stay by Pacific Gas and Electric Company regarding proceedings before the Federal Power Commission entitled and numbered *In Re Pacific Gas and Electric Company,* Docket No. E-6482, and *In Re Sierra Pacific Power Company,* Docket No. E-6697.

On Monday, September 23, 1957 in the course of the oral argument of certain motions in a separate action brought by Sierra Pacific Power Company against Pacific Gas and Electric Company in the United States District Court for the Northern District of California, Southern Division

(Civil No. 35591), counsel for Pacific Gas and Electric Company stated that his client intends to file in your Court a petition, under Section 313(b) of the Federal Power Act, for review of the Federal Power Commission's final order in proceedings above referred to. The last day on which such a petition could be filed is November 5, 1957.

As will necessarily appear on the face of any such petition for review that may be filed, the order to be reviewed was entered in response to a mandate issued by the United States Court of Appeals for the District of Columbia Circuit, in compliance with the decision of the Supreme Court of the United States in *Federal Power Commission* v. *Sierra Pacific Power Co.,* 350 U. S. 348 (1956), affirming *Sierra Pacific Power Co.* v. *Federal Power Commission,* 223 F 2d 605 (D.C. Cir. 1955). The law seems well established that a petition to review such an order can only be filed in the court which issued the mandate. That court having taken jurisdiction of the controversy, no other Circuit Court would have jurisdiction to entertain the petition, despite the provisions of Section 313(b) of the Federal Power Act. *Morris* v. *Securities and Exchange Commission,* 116 F 2d 896 (2d Cir. 1941); cf. *Hicks* v. *National Labor Relations Board,* 100 F 2d 804 (4th Cir. 1939).

I am not clear whether this is the type of jurisdictional defect which, as it would appear on the face of the petition itself, would move your Court to dismiss the appeal *sua sponte,* or whether Sierra should make a motion to intervene and dismiss the appeal. In any event I would appreciate it very much if you would notify Messrs. Brobeck, Phleger & Harrison immediately if any attempt is made to file such a petition in your Court. I am sending a copy of

this letter to Mr. Searls, counsel for Pacific Gas and Electric Company, and to Mr. Wahrenbrock, Solicitor for the Federal Power Commission for their information.

Respectfully,

William C. Chanler
Of Counsel for
Sierra Pacific Power Company

cc. F. T. Searls, Esq.
Howard E. Wahrenbrock, Esq.

Gregory A. Harrison, Esq.
Brobeck, Phleger & Harrison